

## SUBCOMMITTEE NO. 3

## Agenda

Chair, Senator Denise Moreno Ducheny  
Senator George C. Runner  
Senator Tom Torlakson



Thursday, April 7, 2005  
(Upon Adjournment)  
John L. Burton Hearing Room (4203)  
Consultant, Anastasia Dodson

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**Please Note:** Only those items and issues contained in this agenda will be discussed at this hearing. Issues pertaining to these items may be reviewed again. Please see the Senate File for dates and times of subsequent hearings.

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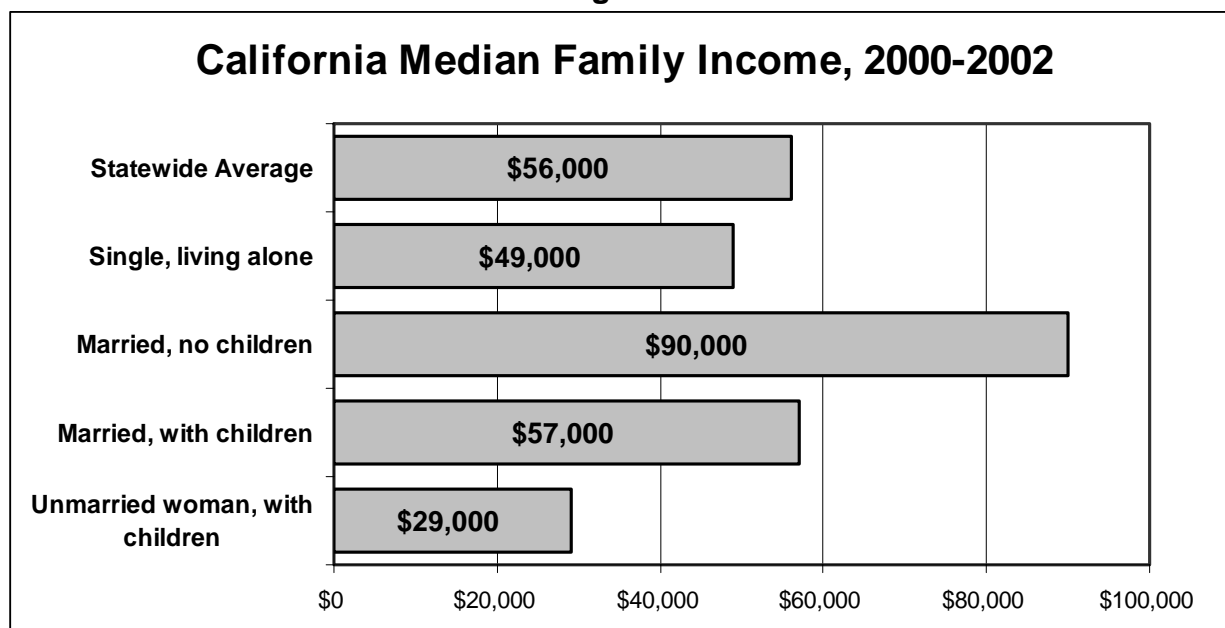
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## 5175 Department of Child Support Services (DCSS)

**Budget Summary:** The Department of Child Support Services (DCSS) administers the child support enforcement program operated by local child support agencies (LCSAs). The budget anticipates collections of \$2.4 billion in the budget year, an increase of 1.7 percent over the current year. The department's overall budget expenditures are proposed to increase by \$279.2 million to \$1.4 billion. Most of the additional funding request is due to the child support automation system penalty (see issue 1 below).

**Mission:** The mission of the Department of Child Support Services is to promote the well-being of children and the self-sufficiency of families by providing child support establishment, collection, and distribution services to help both parents meet the needs of their children.

Figure 1



Source: Public Policy Institute of California, *Recent Trends in Income and Poverty*, February 2004

**Children and Families in Poverty:** Child support can help mitigate the low income and high poverty rates for children and families headed by single women. As shown in Figure 1 above, median family income for unmarried women with children is \$29,000 per year, slightly more than half of the married with children family income level. Over 1.7 million California children (18.6%) live in poverty. California ranks 38th out of 50 states and the District of Columbia in child poverty, despite having the 11th highest median family income. Thirty-two percent of female-headed households in the state were living in poverty in 2003. (The federal poverty level was \$15,260 for a family of three in 2003.)

**DCSS Issue 1: California Child Support Automation System (CCSAS)  
Federal Penalty**

**Description:** Since 1997, California has been subject to substantial federal penalties due to the state's failure to establish a single statewide system for the collection of child support. The cumulative federal penalty from 1998 through 2006 is expected to be over \$1.2 billion General Fund. The automation system is scheduled to be completed and implemented statewide by 2008.

**Background:**

- **\$218 Million Federal Penalty in Governor's Budget:** The budget includes \$218 million General Fund in 2005-06 for the federal fiscal year (FFY) 2005 penalty. The 2004 Budget Act did not include funding for this penalty, as the payment was entirely deferred to state fiscal year 2005-06. The federal government recently informed the department that payment of the FFY 2006 penalty will be deferred to 2006-07. The penalty amount is a percentage of program administration costs, with an increasing percentage each year. California has reached the maximum percentage level at 30 percent of administrative costs.
- **2005 Penalty Reduction Denied:** During 2004 budget hearings, the department indicated that federal certification of automation system compliance might be possible as early as September 2005. If approved this would have reduced the 2005-06 penalty by 90 percent. Based on an October 2004 letter from the federal government, the department now indicates certification and penalty relief are not expected until September 2006.

**Questions:**

1. DCSS, when does the Administration expect that the federal penalty will be reduced? In what year does the Administration expect to make the final federal penalty payment?
2. DCSS, has the Administration requested from the federal government that the state be allowed to reinvest the penalty in child support program activities?

**DCSS Issue 2: CCSAS Governor's Budget Augmentations**

**Description:** The Governor's Budget proposes \$267 million (\$92 million General Fund) for the continued development of CCSAS, including an augmentation of \$90 million (\$25 million General Fund) above the current year. This includes funding for both the CCSAS Child Support Enforcement (CSE) component and the State Disbursement Unit (SDU) component. The Franchise Tax Board (FTB) acts as DCSS' agent for the procurement, development and maintenance of the CCSAS project. Due to Legislative concerns, recent CSE contract amendments have been renegotiated to include deliverable-based payment conditions.

**Background:**

- **CCSAS Child Support Enforcement (CSE) Component:** The CSE component of CCSAS will provide a statewide central database for case management, financial management, and interstate communication. The budget proposes to redirect 1.5 existing DCSS positions and reestablish 1.5 expiring limited-term positions to implement the CSE component. Total costs for the CSE are projected to be \$1.3 billion (\$466 million General Fund) from 2003-04 through 2012-13. This component is scheduled to be completed by September 2008.
- **CCSAS State Disbursement Unit (SDU) Component:** The SDU component of CCSAS will provide statewide collections and electronic disbursement. The budget proposes 37.0 additional positions (10.5 new and 26.5 redirected) for SDU project development and operations. Total costs for the SDU are projected to be \$217 million (\$76 million General Fund) from December 2004 through December 2011. This component is scheduled to be completed by September 2006.
- **Redirected Positions:** The Administration's proposal to redirect 29.5 positions includes 13.0 expiring limited-term positions that were originally established for the Compromise of Arrears program. The department indicates that the remaining 16.5 positions were redirected from non-CCSAS project positions, and from non-critical mission areas that would allow the department to still meet state and federal requirements at a reduced level. The areas of redirection include Forms and Outreach, Quality Assurance, Data and Performance Analysis, California Parent Locator Services, Accounting and Fiscal Services, and Business Services. The department indicates that it is committed to the CCSAS SDU project and plans to do what is necessary to ensure the successful development and implementation is completed in a timely manner.
- **Trailer Bill Language for SDU General Fund Loan Authority:** The budget also includes trailer bill language that would authorize DCSS to borrow up to \$150 million from the General Fund to ensure timely disbursement of child support payments.

The department indicates this loan authority is necessary to rule out potential delays in moving collections through the State Treasury system. It will take a minimum of two days to move collections through the State Treasury system to the Service Provider (Bank of America). This process can take longer depending on the timing of when remittances are received and processed by the State Treasurer. Additionally, the loan authority would cover fund liabilities such as non-sufficient fund (NSF) checks and IRS negative adjustments.

The department also indicates that failing to process collections within two days would result in non-compliance with the federally mandated child support payment deadline of two days, which could lead to federal penalties and the loss of federal incentive funds. Also, delayed payments could create financial hardships for families that depend upon these payments for basic living expenses and could result in significant dissatisfaction among child support clients, especially the non-IV-D population who will be receiving child support payments from the State for the first time once the CCSAS is implemented.

- **Contract Amendments Renegotiated Due to Legislative Concerns:** In November 2004 the Department of Finance submitted a request to the Legislature to increase project contract costs by \$14 million in 2005-06 to implement the initial phase of the automation system more quickly. However, the November 2004 proposed contract amendments were not consistent with prior Legislative intent, as they did not specify performance- or deliverable-based payment conditions. In response to concerns expressed by the Legislature in December 2004, the Administration indicates it has amended the contract to include those payment conditions.

### Questions:

1. LAO, please describe the \$14 million contract amendments proposed by the Administration in November 2004, and why the structure of these amendments was not consistent with Legislative intent.
2. FTB, please briefly describe the performance-based contract amendments that were recently negotiated in response to Legislative concerns.
3. DCSS, please describe the impact of the proposed redirection of 29.5 positions, including 13.0 positions redirected from the Compromise of Arrears Program. Will redirecting these positions reduce child support revenue collection efforts?

### DCSS Issue 3: Federal Performance Measures

**Description:** The state receives federal financial incentives and penalties based on five child support performance measures. In FFY 2002 California's average score ranked 41<sup>st</sup> among 54 states and territories, and scored lower than the national average on three out of five measures. The budget estimates only a 1.7 percent increase in collections in 2005-06.

In addition, approximately \$19 billion in child support arrears is currently owed to families in the state. An analysis conducted by the Urban Institute found that approximately \$4.8 billion of the state's arrears is collectable, including \$2.3 billion of which is owed to the state for CalWORKs reimbursements.

### Background:

**Figure 2**

<b>Federal Performance Measure</b>	<b>National FFY 2003</b>	<b>California FFY 2004</b>	<b>Federal Minimum Standard</b>
IV-D Paternity Establishment	77%	<b>88%</b>	50%
Support Orders Established	72%	<b>78%</b>	50%
Collections on Current Support	58%	<b>48%</b>	40%
Collections on Arrears	60%	<b>55%</b>	40%
Cost-Effectiveness Ratio	\$4.33	<b>\$2.12</b>	\$2.00

**Cost-Effectiveness:** California's child support system collected \$2.12 in revenue for every \$1.00 spent on collection efforts in federal fiscal year 2004. This is significantly lower than the national average of \$4.33 in revenue per dollar spent. Among 54 states and territories, California ranks 49<sup>th</sup> in cost-effectiveness.

The California Child Support Directors Association indicates that the following factors contribute to the state's relatively poor cost-effectiveness ratio:

- **Automation Projects Still in Development:** California is still spending significant resources on CCSAS development and legacy automation costs. All but two other states no longer have major automation development costs.
- **Judicial Child Support Model:** California has a court-based child support system that that Association indicates is more expensive than the administratively based systems used in many other states.
- **Uncollectable Arrears:** Much of the child support arrears is owed by low-income non-custodial parents. According to a March 2003 report prepared for the department, 25 percent of debtors have no recent income, 36 percent have net annual income of \$10,000 or less, and only 1 percent have net annual income over \$50,000. In addition, California has a disproportionate share of the nation's child support arrears – 12 percent of the nation's child support caseload, vs. 20 percent of the nation's arrears.
- **Caseload Composition (CalWORKs vs. non-CalWORKs cases):** Child support collections are generally lower for families that have or are currently receiving CalWORKs, as the non-custodial parent is more likely to be low-income. California has a higher proportion of child support families that are current or former CalWORKs recipients than other states. However, an analysis of individual county cost-effectiveness conducted by the department last year found that a high proportion CalWORKs families in a county did not necessarily result in proportionately higher county costs.
- **Lack of Universal Caseload Model:** Three states require all parents to make child support payments through the state's child support system. The Association indicates that states with universal caseloads are more cost-effective because they have more cases with higher orders that are more likely to pay voluntarily or via wage assignment.

**Child Support for CalWORKs Leavers:** A recent MDRC report <sup>1</sup> concludes that when families receive child support, it is an important contributor to their overall income, and it generally takes on more importance in the family budget after women leave welfare. However, the report also indicates that too few families receive child support, and it can be a fairly

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<sup>1</sup> MDRC. *The Interaction of Child Support and TANF: Evidence from Samples of Current and Former Welfare Recipients*, January 2005.

unreliable source of income, at least on a monthly basis. Receipt rates and award rates are lower in general for current and former recipients than for all eligible women.

The department indicates that all CalWORKs recipients are automatically eligible to continue receiving child support services at no cost after leaving CalWORKs. Local Child Support Agencies (LCSAs) notify custodial parents continuing child support services are available at no cost, and the custodial parent is advised to contact the LCSA. The existing case remains open, and parents are not required to reapply for child support services.

The department indicates that child support services are discontinued **only** when the custodial parent fails to respond to the LCSA notice or declines continuing support services. The LCSA verifies, in writing, the custodial parent's intentions to decline child support services. However, if welfare arrears, owed to the state, have accrued and the parent has declined continuing services, the LCSA is required to continue to enforce and collect the arrears. Custodial parents declining continuing services receive information concerning future child support needs, including the option at any time to have their child support case re-opened.

**Collections on Arrears:** Approximately \$19 billion in child support arrears is currently owed to families in the state. An analysis conducted by the Urban Institute found that approximately \$4.8 billion of the state's arrears is collectable, including \$2.3 billion of which is owed to the state for CalWORKs reimbursements.

The Compromise of Arrears Program (COAP) was established in 2003-04 to offer reduced lump sum settlements to parents in exchange for their commitment to make ongoing payments. This program is also intended to reconnect families estranged due to unresolved child support payments. The DCSS indicates that due to automation system constraints, this program cannot be implemented as initially designed. The budget proposes to retool the program and extend 9.0 of the 22.0 positions initially provided for this program. The remaining positions are proposed to be redirected to CCSAS in the Governor's Budget, including 8.0 currently vacant positions.

**\$2.3 Billion in Uncollected Arrears:** The amount of arrears collected under COAP has been significantly less than originally estimated. The Governor's budget estimates that of the \$2.3 billion in collectable child support arrears owed to the state for CalWORKs families, approximately \$6 million will be collected in the current year and \$12 million will be collected in the budget year as a result of COAP. The original estimate of COAP collections was \$50 million annually.

#### **Questions:**

1. DCSS, please explain why the state's cost-effectiveness ratio is significantly lower than the national average. How does the Administration propose to improve the state's low cost-effectiveness ratio?
2. DCSS, please describe the status of the COAP, and why original revenue estimates were not achieved.

**DCSS Issue 4: Local Child Support Funding**

**Description:** The Governor's Budget proposes to continue holding local child support funding flat at \$710 million (\$194 million General Fund) in 2005-06. The relationship between local funding and collections was discussed in last year's budget hearings, but is still not entirely clear. The Legislative Analyst's Office recommends that the department lead a workgroup to develop a consistent local administrative cost reporting methodology. The Child Support Directors Association suggests that an administrative cost methodology be developed by January 2006.

**Background:**

**Local Child Support Agency (LCSA) Functions:** Local child support agencies are responsible for the administration of child support programs at the county level and perform functions necessary to establish and collect child support. Program activities include establishing child support cases, establishing child support orders, collecting current and past-due child support, enforcing medical support orders, and implementing customer service initiatives.

**LCSA Funding Structure:** California provides baseline compensation to counties, on a statewide basis, at a level comparable to 13.6% of the estimated level of collections adjusted to reflect county expenditures and available General Fund resources. The DCSS allocates resources for administration of local child support programs in a lump sum and does not control county expenditures for program activities and for child support initiatives.

Baseline county funding for the implementation of local child support programs is established according to a statutory formula based on child support collections. Individual county allocations are generally based on historic county expenditures and vary across the state.

**Allocation Relationship to Performance:** In recent years, the Legislature has considered the effect on program performance of child support administrative funding reductions, and the relationship of existing allocations to program performance and actual costs. No statewide consensus has been reached, although some data suggests that California can improve its performance without investing new resources in the child support program if under-performing local agencies improve their performance.

**LCSA Staffing Reductions:** The Child Support Directors Association reports that state and local staffing has declined from 11,070 in 2001-02 to 9,319 in 2003-04, due to the lack of funding increases. Additional local positions may be eliminated or held vacant in 2005-06 as a result of flat funding. Some counties indicate that flat funding may prevent revenue collections from increasing in 2005-06.

**LAO Proposal:** The Legislative Analyst's Office (LAO) reviewed local cost reports and initially recommended that local funding for administrative activities be limited to 25 percent of each county's total allocation in 2005-06. However, further review found that counties did not receive sufficient information to ensure consistent reporting of administrative costs. The LAO



now notes an alternate proposal, that the department may instead lead a workgroup to develop a consistent local administrative cost reporting methodology.

**Questions:**

- 1 DCSS, please present the Governor's Budget proposal to hold local child support funding flat in 2005-06. How would this proposal affect LCSA staffing levels and collections levels?
- 2 LAO, please present your recommendation for administrative cost reporting.
- 3 DCSS, how does the department propose to ensure that local administrative costs are consistently reported? Do you concur with the LAO's recommendation?

**Recommendation:** Reduce the DCSS state operations appropriation by \$50,000 General Fund, and adopt placeholder budget bill language to restore this appropriation if the department submits a report to the Legislature by November 1, 2005 with recommendations for a consistent statewide LCSA cost reporting methodology.

**5180 Department of Social Services (DSS)**

**CalWORKs Program Description.** The California Work Opportunity and Responsibility to Kids (CalWORKs) program provides cash benefits and welfare-to-work services to low-income children and their parents or caretaker relatives. The average family of three must have an annual net income below \$12,389, or 77 percent of the federal poverty level (FPL), in a low-cost county to be eligible for CalWORKs. A family of three in a high cost county must have income below 81 percent of the FPL to be eligible for CalWORKs. Parents are required to work or participate in work-related activities for at least 32 hours per week, and income above \$225 per month offsets a portion of the grant. Adults have a lifetime limit of five years (60 months) in CalWORKs.

**Enrollment Summary.** After peaking in March of 1995, CalWORKs enrollment dropped by 48 percent through 2004. Enrollment decreased by 33 percent since CalWORKs replaced the former Aid to Families with Dependent Children (AFDC) program in 1998. The caseload decline is due to a combination of demographic trends (such as decreasing birth rates for young women), California's economic expansion, and full implementation of welfare reform. After years of declines, enrollment bottomed out in 2003-04, and is projected to increase by 1.9 percent in 2004-05.

The budget proposes significant reductions in the CalWORKs program, resulting in a caseload decrease of 0.8 percent below the current year. The department estimates CalWORKs average monthly caseload will be 472,786 families in 2005-06, which includes almost 961,000 children (see Figure 3 below). Without the proposed reductions, average monthly enrollment would have been 486,425 families in 2005-06.

**Figure 3**

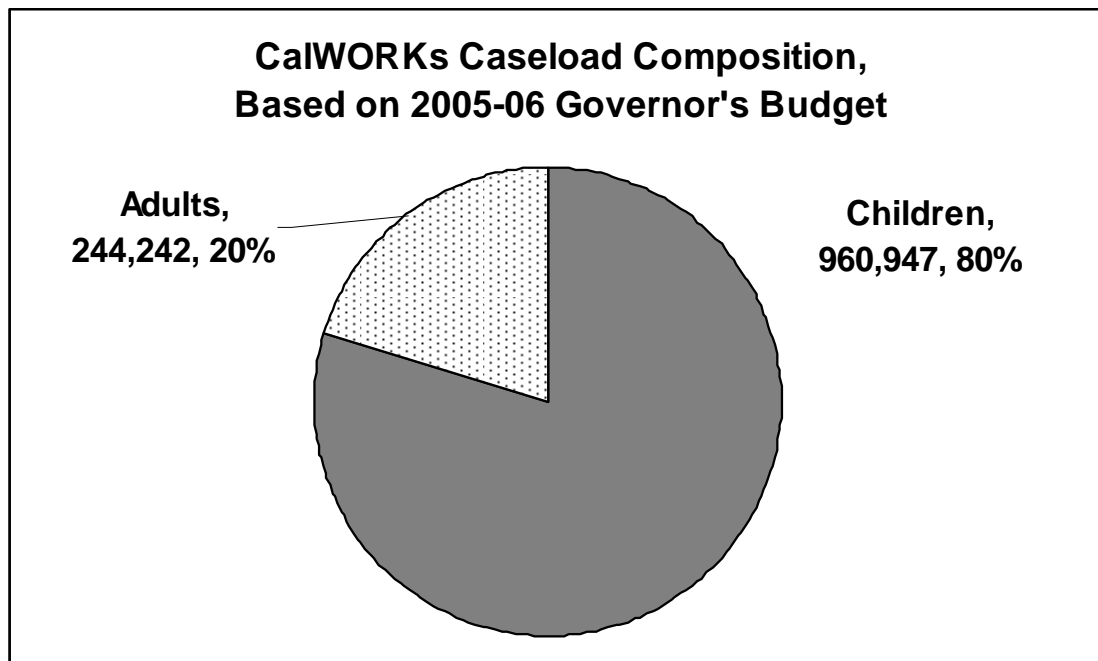
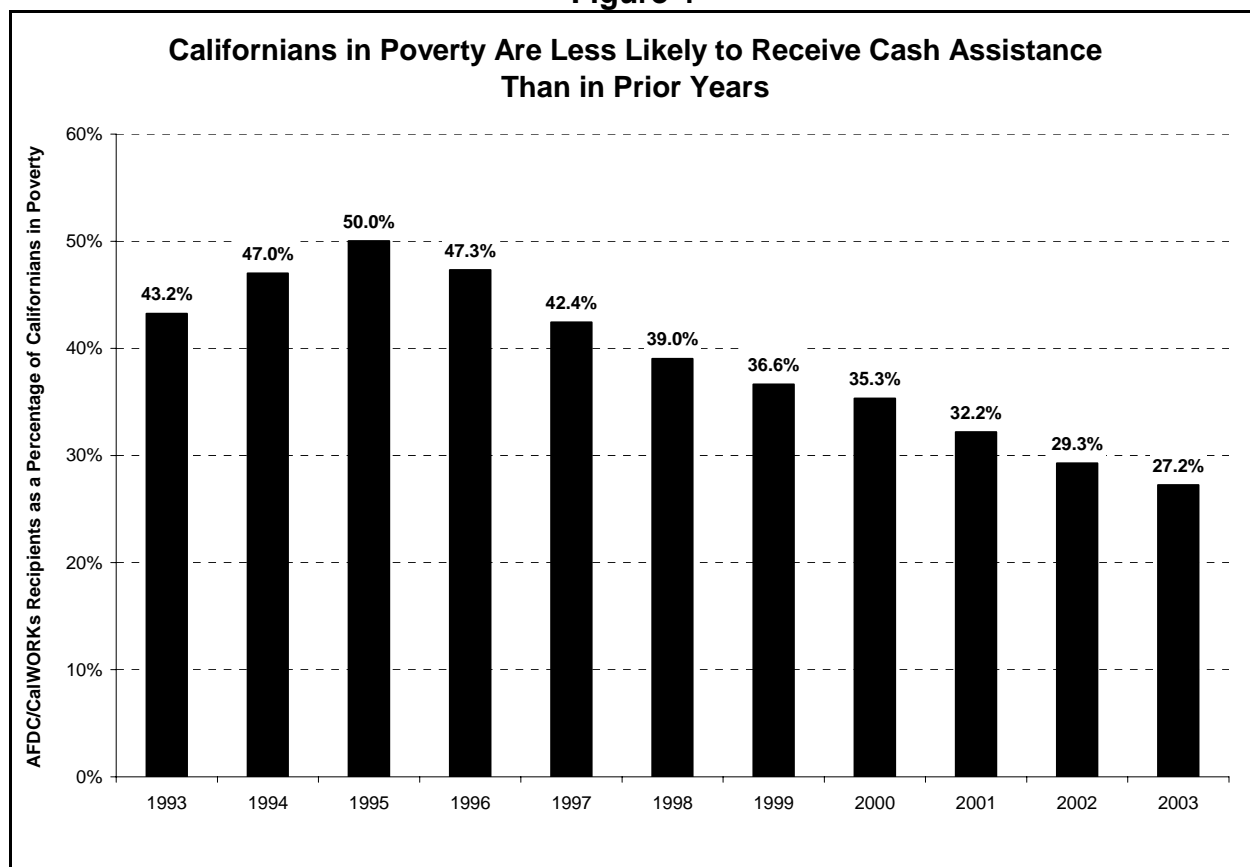


Figure 4



*Source: California Budget Project*

While welfare enrollment has decreased since 1995, Figure 4 above shows that during that same period low-income Californians have become less likely to receive cash assistance. This is partly the result of many families leaving CalWORKs and remaining in low-wage employment.

**Proposed Reductions:** The Governor's Budget includes a total of \$582 million in reductions to the CalWORKs program in 2005-06:

- **Reduce CalWORKs Grants by 6.5 percent.** The budget proposes to reduce CalWORKs grants by approximately 6.5 percent, resulting in savings of \$212 million. For a typical family of three, the maximum grant would be reduced from \$723 to \$676 per month.
- **Eliminate CalWORKs Cost of Living Adjustment (COLA).** The budget proposes to suspend the July 2005 COLA, and permanently suspend all future CalWORKs COLAs, resulting in savings of \$143 million.
- **Reduce Earned Income Disregard.** The budget proposes to reduce the Earned Income Disregard for CalWORKs families, resulting in \$82 million savings.

- **Increase Sanctions and Work Requirements.** The budget proposes to expand the CalWORKs work participation reforms based a pending evaluation of CalWORKs sanction policies, for estimated savings of \$12 million.
- **Reduce Employment Services Funding.** The budget proposes to eliminate \$50 million in 2005-06 that was included in the 2004 Budget Act for CalWORKs employment services.
- **Child Care Reform.** The budget proposes to reduce license-exempt child care reimbursement levels, and establish a tiered reimbursement structure for all child care providers, resulting in savings of \$61 million in the DSS, and \$53 million Prop 98 savings in the California Department of Education (CDE).
- **County Pay for Performance Proposal.** The budget proposes to tie county administration funding to CalWORKs client work participation rates, for projected savings of \$22 million.

### **DSS Issue 1: CalWORKs Funding Structure**

**Description:** The Governor's Budget proposes to transfer \$316 million in federal Temporary Assistance for Needy Families (TANF) funds from the CalWORKs program to other areas of the budget. The budget also proposes to count an additional \$201 million General Fund in existing expenditures in the California Department of Education's budget toward the state's TANF Maintenance of Effort (MOE) requirement, instead of funding the CalWORKs program.

#### **Background:**

**CalWORKs Funding Summary.** CalWORKs is funded through an annual federal Temporary Assistance for Needy Families (TANF) block grant of \$3.7 billion, plus \$2.7 billion in state funds to meet a federal Maintenance of Effort (MOE) requirement. The state's MOE is based on welfare spending in 1994, adjusted downward for achievement of certain work participation goals. As a matter of policy, California has chosen to treat the MOE level as a ceiling for General Fund CalWORKs spending. Federal law requires states to spend TANF funds on current and former welfare recipients, with limited exceptions. Accordingly, California spends most federal TANF funds on CalWORKs, and directs some TANF and state MOE funding to activities in other departments.

**TANF Funding for Non-CalWORKs Programs.** Over time, California has broadened its definition of expenditures that can be considered to meet the state's MOE. Additionally, the state has transferred a growing amount of TANF funds to non-CalWORKs programs. As a result, available TANF and MOE funding for the CalWORKs program had been substantially declining.

The 2004 Budget Act addressed this issue through the elimination of TANF funds for juvenile probation services, reduction of most TANF transfers to Title XX, and changing the definition of

child care expenditures counted toward the MOE. The Governor's Budget proposes to reverse the decisions made in 2004-05.

The budget proposes total TANF/MOE funding of \$5.9 billion (\$4.7 billion of which will be spent on the CalWORKs program and \$1.2 billion to support non-CalWORKs federally allowable activities). This constitutes a \$528 million, or 10 percent decrease in CalWORKs expenditures from the current year. As shown in Figure 5 below, total funding for the CalWORKs program has decreased by \$707 million since 1998-99.

**Figure 5: Federal TANF and State MOE Funding for CalWORKs and Other Programs**

	FY 1998-99	2004-05 Governor's Budget	2005-06 Governor's Budget	98-99 to 05-06	
<b>Total TANF Grant/Required MOE</b>	<b>6,640,971,000</b>	<b>6,401,487,000</b>	<b>6,393,328,000</b>	<b>-247,643,000</b>	<b>-3.73%</b>
<b>CalWORKs Program (Actuals)</b>	<b>5,452,464,887</b>	<b>5,273,999,000</b>	<b>4,745,760,000</b>	<b>-706,704,887</b>	<b>-12.96%</b>
Grants	3,728,895,597	3,350,291,000	2,904,332,000	<b>-824,563,597</b>	-22.11%
Administration	518,317,463	500,519,855	477,958,234	<b>-40,359,229</b>	-7.79%
Services	450,275,279	767,713,739	733,107,986	<b>282,832,707</b>	62.81%
Child Care	360,733,329	549,370,406	524,606,779	<b>163,873,450</b>	45.43%
Substance Abuse/Mental Health Svcs	21,212,219	106,104,000	105,755,000	<b>84,542,781</b>	398.56%
County Share of Admin/Svcs*	80,807,136	61,692,000	62,638,000	<b>-18,169,136</b>	
Performance Incentives(budgeted)	373,031,000			<b>-373,031,000</b>	-100.00%
				<b>0</b>	
<b>Probation</b>	<b>201,413,000</b>	<b>67,138,000</b>	<b>201,413,000</b>	<b>0</b>	<b>0.00%</b>
<b>KinGAP</b>	<b>0</b>	<b>95,557,000</b>	<b>102,930,000</b>	<b>102,930,000</b>	
				<b>0</b>	
<b>Non-CalWORKs MOE in CDSS</b>	<b>(11,269,000)</b>	<b>(10,322,000)</b>	<b>(10,129,000)</b>	<b>1,140,000</b>	<b>-10.12%</b>
<b>Other MOE in CDSS</b>	<b>305,663,000</b>	<b>324,819,000</b>	<b>307,290,000</b>	<b>1,627,000</b>	<b>0.53%</b>
<b>MOE In Other Department Budgets</b>	<b>402,839,000</b>	<b>293,218,000</b>	<b>495,938,000</b>	<b>93,099,000</b>	<b>23.11%</b>
<b>State Support</b>	<b>29,016,000</b>	<b>26,262,000</b>	<b>26,206,000</b>	<b>-2,810,000</b>	<b>-9.68%</b>
				<b>0</b>	
<b>Total Expenditures</b>	<b>6,380,126,887</b>	<b>6,070,671,000</b>	<b>5,869,408,000</b>	<b>-510,718,887</b>	<b>-8.00%</b>
Federal TANF	3,472,973,887	3,403,002,000	3,209,898,000	<b>-263,075,887</b>	-7.57%
General Fund	2,733,123,474	2,467,210,000	2,464,886,000	<b>-268,237,474</b>	-9.81%
Other State Funds (ETF, Prop 10)	0	40,084,000	40,119,000	<b>40,119,000</b>	
County Funds	174,029,526	160,375,000	154,505,000	<b>-19,524,526</b>	-11.22%
				<b>0</b>	
<b>Total TANF transfers</b>	<b>284,965,000</b>	<b>544,555,000</b>	<b>839,471,000</b>	<b>554,506,000</b>	<b>194.59%</b>
Non-CalWORKs Transfers	0	63,099,000	179,892,000	<b>179,892,000</b>	
Transfers to Stage 2, Tribal TANF and Reserve	284,965,000	481,456,000	659,579,000	<b>374,614,000</b>	131.46%
TANF Grant/Required MOE	6,640,971,000	<b>6,401,487,000</b>	<b>6,393,328,000</b>	<b>-247,643,000</b>	-3.73%
Prior Year TANF Carryforward	617,020,000	522,246,000	315,551,000	<b>-301,469,000</b>	-48.86%
Unspent Performance Incentives				<b>0</b>	
High Performance Bonus		7,044,000		<b>0</b>	
<b>Total Available Funding</b>	<b>7,257,991,000</b>	<b>6,930,777,000</b>	<b>6,708,879,000</b>	<b>-549,112,000</b>	<b>-7.57%</b>
<b>Total TANF/MOE Expends</b>	<b>6,665,091,887</b>	<b>6,615,226,000</b>	<b>6,708,879,000</b>	<b>43,787,113</b>	<b>0.66%</b>
NET TANF Carry-over Funds	592,899,113	315,551,000	0	<b>-592,899,113</b>	-100.00%
				<b>0</b>	
CalWORKs contribution to the General Fund	708,502,000	956,757,000	1,265,948,000	<b>557,446,000</b>	78.68%

**New TANF or MOE Transfers:** The Governor's Budget proposes to increase TANF fund transfers to non-CalWORKs activities and count additional funding in non-CalWORKs programs toward the MOE. Reducing the TANF or MOE funding from these programs would require a corresponding General Fund backfill to maintain total funding for these programs at the level proposed in the budget.

- **\$55 million TANF to the Foster Care program.** Administration indicates trailer bill language is necessary, and is proposed. Denied by the Legislature last year.
- **\$60 million TANF to the Department of Developmental Services.** Administration indicates trailer bill language is not necessary. Denied by the Legislature last year.
- **\$201 million TANF to Juvenile Probation Facilities.** Administration indicates trailer bill language is not necessary. However, last year the Administration indicated that TANF funding for juvenile probation would not be continued due to the November 1, 2004 sunset of the Comprehensive Youth Services Act. The Administration now contends that this TANF transfer may be achieved under a Memorandum of Understanding between DSS and the Board of Corrections. Continuation of this TANF transfer past November 1, 2004 was denied by the Legislature last year.
- **\$201 million General Fund in existing California Department of Education child care funding counted toward the MOE.** Administration indicates trailer bill language not necessary. Although a portion of the \$201 million in additional MOE is due to caseload changes, the majority of this funding is shifted MOE from the CalWORKs program.

**Questions:**

1. LAO, please briefly describe the federal TANF MOE requirement and CalWORKs program funding structure. What has happened to CalWORKs funding as share of TANF/MOE over time, and how has that affected the program?
2. DSS, how much TANF and MOE funding is proposed to be shifted to other programs from CalWORKs in 2005-06, compared to 2004-05?
3. DSS, how does this amount compare to the funding reductions proposed for the CalWORKs grant reduction, suspension of the CalWORKs COLA, and reduction of the earned income disregard?

**DSS Issue 2: CalWORKs Grant Reduction and Cost of Living Adjustment (COLA) Suspensions**

**Description:** The budget proposes to reduce CalWORKs grants by 6.5 percent, suspend the July 2005 CalWORKs COLA, and permanently suspend all future COLAs, for combined savings of \$355 million in 2005-06. The budget also proposes trailer bill language so that should the state lose its appeal of the *Guillen v. Schwarzenegger* case (which addresses the October 2003 CalWORKs COLAs and the vehicle license fee changes made by the Governor), a COLA would only be provided retroactively from October 2003 through the effective date of the trailer bill, and not provided in the future. By eliminating CalWORKs eligibility for some working families, this proposal may reduce the state's federal work participation rate.

**Background:**

**Maximum Aid Payment (MAP) would be Reduced:** The proposed CalWORKs grant changes would have a combined effect of reducing the maximum monthly grant for a family of three with no earnings from \$723 to \$676, a reduction of \$47 per month. The reduction would be partially offset by an increase in Food Stamp benefits. In general, Food Stamp increases offset about 45 percent of the proposed grant reductions.

The proposed maximum grant level of \$676 per month is \$18 lower than the amount provided to AFDC recipients in 1989. At the same time, the purchasing power of the grant in 2005-06 would be 60.5 percent of the 1989 level. Absent the 6.5 percent reduction, the July 2005 COLA would have increased the maximum CalWORKs grant to \$752 per month for a family of three.

**Average Aid Payment for Working Families would be Reduced:** Actual grants for families vary depending on family size and household income. Families that work or have other income receive grants lower than the MAP. The projected average grant for all families for 2004-05 is \$555 and for 2005-06 is \$501.

The average CalWORKs grant for a working family of three without any proposed reductions is approximately \$395 (not including the July 2005 COLA). The proposed grant reduction would reduce that average grant by \$47, and the proposed decrease in the earned income disregard (see Issue 3 below) would further reduce the average grant for working families by \$80 per month. Therefore, the combined average grant reduction for working CalWORKs families is about \$127 (this reduction would be partially offset by an increase of about \$58 in Food Stamp benefits).

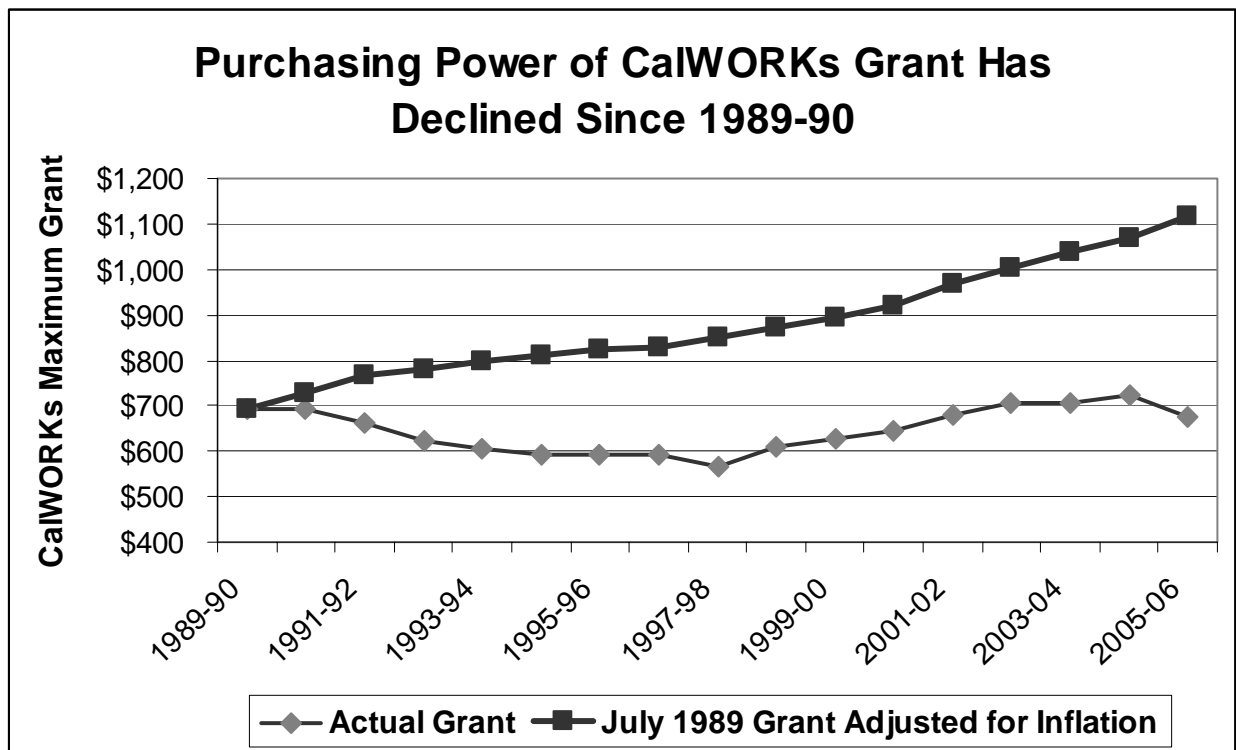
**Working Families Ineligible for CalWORKs:** In addition to decreasing resources available to low-income families, the grant reductions and decrease in the earned income disregard will make 13,639 working families ineligible for CalWORKs cash assistance, a caseload reduction of 2.8 percent. The average monthly number of children in families that would no longer receive grants is 35,092.

The families that would lose eligibility for CalWORKs under these proposals would be working families with earnings that exceed the reduced CalWORKs limit. These families may still be

eligible for health coverage under Medi-Cal and Food Stamps for a period of time, depending on their income level.

**Impact on CalWORKs Work Participation Rate:** The department indicates that California may have trouble meeting the revised federal work participation rate under certain versions of federal TANF reauthorization bills that are currently pending in Congress. Failure to meet required work participation rates may result in federal sanctions. However, the families that would lose CalWORKs eligibility under this proposal are working families that would help the state maintain a higher federal work participation rate.

**Figure 6**



As shown in Figure 6 above, since 1990 the net result of suspended COLAs and reductions to CalWORKs grants have reduced the purchasing power of the grant by 39.5 percent.

**Grant Payments Compared to Other States and Housing Costs:** The Administration indicates that even with these actions, California's grant payment would remain the fourth highest of all 50 states and the second highest of the 10 most populous states.

However, CalWORKs recipients spend much of their grants on rent, due to the high cost of housing in California. According to the U.S. Department of Housing and Urban Development (HUD), fair market rents for a one-bedroom apartment in California average \$904 per month and range from \$425 in Glenn County to \$1,229 in San Francisco County. The proposed maximum monthly grant is \$676 for a family of three.



Figure 7

State	1 Bedroom Rent	Current MAP	Current Rent Gap	Rent Gap with Proposed MAP	Proposed MAP/Rent
California	\$902	\$723	-\$179	-\$226	75%
Ohio	\$505	\$579	\$74	\$74	115%
Pennsylvania	\$596	\$606	\$10	\$10	102%
Michigan	\$587	\$593	\$6	\$6	101%
Texas	\$590	\$579	-\$11	-\$11	98%
Illinois	\$696	\$579	-\$117	-\$117	83%
Georgia	\$651	\$579	-\$72	-\$72	89%
Florida	\$674	\$579	-\$95	-\$95	86%
New York	\$832	\$666	-\$166	-\$166	80%
New Jersey	\$905	\$610	-\$295	-\$295	67%

**Rent Gap Currently \$179, But Would Increase to \$226:** As shown in Figure 7 above, California's current CalWORKs grant (MAP) is \$179 less than the average fair market rent for a one-bedroom apartment in the state. Among the ten largest states, California currently has the second-highest rent gap. In Ohio, Pennsylvania, and Michigan, grants are actually higher than the one-bedroom fair market rate. Under the Governor's proposed grant reduction, the rent gap would increase to \$226, and the maximum grant would decline to only 75 percent of the average rent for a one-bedroom apartment.

Subsidized housing is not available for all qualifying families. According to a National Low Income Housing Coalition report on large public housing authority waiting lists, the 14 California housing authorities that reported in the survey had a total of 454,515 applicants on the waiting lists. Nationally, the federal Department of Health and Human Services reports that just 20 percent of TANF recipients receive subsidized housing. HUD figures from the late 1990's indicate that in California, 10 to 12 percent of TANF recipients used subsidized housing.

**October 2003 COLA Litigation:** In the *Guillen* court case, advocates for the state's CalWORKs recipients successfully argued in superior court that the state should provide the October CalWORKs COLA, since the Governor reduced the Vehicle License Fee (VLF). Currently, the administration is appealing this ruling and an appellate court decision is expected sometime during the second half of 2005. The Administration is proposing trailer bill language to delete the October 2003 COLA in the event that the state loses its appeal. If the *Guillen* ruling is affirmed by the appeals court, the proposed trailer bill language would result in avoided costs of \$131 million in 2005-06, although the state would face a budget risk of \$222 million in retroactive payments to CalWORKs families.

#### Questions:

1. DSS, please present the grant reduction and COLA suspension proposals. How much notification to recipients is required before the grant reduction could be implemented?

2. DSS, how would this proposal affect recipients? How would recipients pay for cost increases in rent, food, and utilities?
3. DSS, how would these proposals affect the state's work participation rate?
4. DSS/DOF, please provide an update on the status of the *Guillen v. Schwarzenegger* court case. Please describe the proposed trailer bill language regarding the October 2003 COLA case.

### DSS Issue 3: Reduce CalWORKs Earned Income Disregard

**Description:** The budget proposes to reduce the Earned Income Disregard for CalWORKs families, resulting in \$79.4 million net savings in 2005-06, and \$109 million in 2006-07. A family of three earning \$1,000 per month would see their monthly grant reduced by \$93, in addition to the grant reduction noted above in Issue 2. By eliminating CalWORKs eligibility for some working families, this proposal may reduce the state's federal work participation rate.

#### **Background:**

**Results of Earned Income Disregards:** The Earned Income Disregard is a key component of the CalWORKs program, as it provides a work incentive for CalWORKs families, but also improves family well-being. National research conducted by MDRC found that earned income disregards increased work, reduced poverty, increased employment retention, and led to improved educational and behavioral outcomes for elementary school-age children. Earlier findings also showed that, in the short-term, income disregards reduced domestic abuse and increased the stability of two-parent relationships.

**Current Law:** The maximum CalWORKs grant is the amount of money a family receives if it has no other income. If the family has income, the grant is reduced after a specified amount of income is not counted (referred to as the income disregard). In order to provide an incentive for CalWORKs recipients to work, current law disregards (does not count) the first \$225 in earned income and 50 percent of each additional dollar earned when determining a family's grant amount.

The LAO provides the following examples to illustrate current law:

- **Family Earning \$225.** Currently, the maximum monthly CalWORKs grant for a family of three in a high-cost county is \$723. Under the current income disregard policy, a family of three who earned \$225 per month would have 100 percent of their earnings disregarded and would receive the maximum grant of \$723 plus their earnings of \$225 for a total income of \$948 per month (excluding food stamps).
- **Family Earning \$1,025.** Figure 8 below shows the disregard and grant calculations for a family of three with \$1,025 in monthly earnings. The top portion of the figure shows that \$625 in earnings will be disregarded for purposes of determining the family's grant and that \$400 will be counted. The bottom portion of the figure calculates the family's grant

by subtracting the \$400 in countable earnings from the maximum grant of \$723 resulting in a grant of \$323. The grant plus earnings would result in total income of \$1,348 per month (excluding food stamps) for this family.

**Figure 8**

<b>CalWORKs Earned Income Disregard Family of Three, \$1,025 in Earnings</b>	
<b>Disregard Calculation</b>	<b>Amount</b>
Earnings	\$1,025
Initial disregard of \$225	225
Remainder	\$800
Apply 50% disregard to remainder	50%
Additional Earnings Disregarded	\$400
Initial disregard from above	225
<b>Total Earnings:</b>	
<b>Disregarded</b>	<b>\$625</b>
<b>Counted</b>	<b>\$400</b>
<b>Grant Calculation</b>	
Maximum grant	\$723
Less countable earnings	400
<b>Grant</b>	<b>\$323</b>

**Governor's Budget Proposal:** The Governor's Budget proposes to reduce the income disregard to \$200 and 40 percent of remaining income, effective October 1, 2005. This proposal would reduce the level at which low-income working families remain eligible for CalWORKs benefits, and would reduce the grants for all working families. This proposal would affect 112,669 families in 2005-06.

**Figure 9**

<b>Impact of Governor's Income Disregard Family of Three High-Cost Counties<sup>a</sup></b>						
<b>Hours/Week, Hourly Wage</b>	<b>Monthly Earned Income</b>	<b>Grant Plus Earnings</b>		<b>Change From Current Law</b>		
		<b>Current Law</b>	<b>Governor's Proposal</b>	<b>Amount</b>	<b>Percent</b>	
10 hours, \$6.75	\$292	\$982	\$960	-\$22	-2.2%	
20 hours, \$6.75	585	1,128	1,077	-51	-4.5	
40 hours, \$6.75	1,169	1,420	1,311	-109	-7.7	
40 hours, \$9.00	1,559	1,615	1,467	-148	-9.2	

a Assumes current \$723 maximum monthly grant.

In Figure 9 above, the LAO provides examples of how the proposed reduction would affect working family income.

The LAO also notes that reducing the income disregard lowers the point at which families would no longer be eligible for a grant. The exit point at which families are no longer eligible for CalWORKs is currently \$1,671 per month for a family of three. Under the Governor's proposal, the exit point for a similar family would drop to \$1,405 per month (108 percent of poverty guideline). Reducing the exit point will mean that about 8,900 families will become ineligible for CalWORKs. Such exiting families, however, would remain eligible for food stamps, child care, and Medi-Cal, so long as their income remains below the eligibility thresholds for these programs.

**Impact of Reducing the Disregard on Work Incentive and Behavior:** The LAO indicates that reducing the disregard could have two impacts on the working behavior of recipients. On the one hand, it could result in a disincentive to work by reducing the amount of income retained from starting work or increasing one's hours of work. Thus, new entrants to CalWORKs who have no income along with currently aided families who are not working would be most affected by this disincentive. On the other hand, reducing the disregard could increase the incentive to work to the extent that families decide to work more hours in order to make up for the grant reduction pursuant to the revised disregard. Families with substantial earnings, but with incomes below the exit point would be most affected by this increase in the incentive. With more hours of work, such a family could make up for the lost income and possibly leave cash assistance. The LAO expects these two effects to in part offset each other.

**Impact on CalWORKs Work Participation Rate:** The department indicates that California may have trouble meeting the revised federal work participation rate under certain versions of federal TANF reauthorization bills that are currently pending in Congress. Failure to meet required work participation rates may result in federal sanctions. However, the families that would lose CalWORKs eligibility under this proposal are working families that would help the state maintain a higher federal work participation rate.

**LAO Options:** The LAO describes two alternatives that would probably increase the work incentive, especially the incentive to work more than half-time. However, the LAO notes that they result in less budgetary savings, and reduce grants for families with the lowest earnings.

- **Disregard All Income at a Constant Percentage Rate.** Given that Illinois has the highest level of work participation among the ten largest states, we first examined their disregard. In Illinois, 67 percent of all income is disregarded; however, there is no minimum income amount which is disregarded at 100 percent. (For example, California disregards 100 percent of the first \$225 in earnings.) Assuming no change in work behavior, adopting a straight 67 percent disregard in California would actually cost more than current law (at least \$40 million per year). It would also raise the exit point for CalWORKs by about \$170 for a family of three. A variant on this approach would be to set the disregard rate at 57 percent. This would keep California's exit point near where it is today and would result in annual savings of about \$65 million compared to current law. (When welfare reform was first debated in 1997, the Wilson administration initially proposed a 54 percent disregard.)

The main advantage of a constant disregard at a rate higher than the current 50 percent is that it creates a stronger incentive to increase earnings as seems to be illustrated by Illinois. For example, a family earning more than \$225 per month who increased their monthly earnings by \$100 would keep \$67 under the Illinois style disregard compared to just \$50 under California's current law. The main disadvantage is that families earning less than \$225 would have less of an incentive to work since they could only keep 67 percent of their earnings (instead of the entire amount under California's system). Consequently, such families would be worse off financially.

- **Disregard More Income at Higher Earnings.** Under this approach the 50 percent disregard would apply to all families, but the 100 percent exclusion on the first \$225 earned would only be provided to families earning \$600 or more per month. Those earning less than \$600 (about 20 hours per week at the minimum wage), would receive a flat disregard of 50 percent, but they would not receive the base 100 percent disregard on their first \$225 in earnings.

The reason for selecting the \$600 amount is that it corresponds to roughly 20 hours of work per week at the minimum wage. Under current law, adult participants must meet a "core" participation hour requirement of 20 hours per week. Unsubsidized employment is one way to meet the core requirement.

This approach would result in annual savings of about \$48 million compared to current law. The advantage is that it would strongly encourage recipients to work at least 20 hours per week, because they would receive the benefit of the \$225 exclusion once their earnings reach \$600 per month. The disadvantage is that it would lower the grants for families with earnings below \$600 per month because until they earned \$600 they would not receive the 100 percent disregard on their first \$225 earned. It would also reduce the incentive for those not working to begin work at less than \$600. It would not change the exit point for CalWORKs in relation to current law.

### Questions:

1. DSS, please present the Governor's proposal. How would this proposal affect work incentives among CalWORKs families?
2. DSS, how would these proposals affect the state's work participation rate?
3. LAO, please describe alternatives to the Governor's earned income disregard proposal.
4. DSS, what are the goals of the CalWORKs program? How well is the program achieving these goals? How would this proposal affect the achievement of those goals?